ORAL ARGUMENT NOT YET SCHEDULED

Nos. 13-5247 & 13-5248

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

STATE NATIONAL BANK OF BIG SPRING, et al.,

and

STATES OF SOUTH CAROLINA, et al.,

Appellants,

v.

JACOB J. LEW, et al.,

Appellees.

On Appeal from the United States District Court for the District of Columbia
No. 1:12-cv-001032-ESH

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* 11 U.S.C. § 726(b) 1, 2

* 11 U.S.C. § 1123(a)(4) 1, 2

* Authorities upon which we chiefly rely are marked with asterisks.

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GLOSSARY

Term	Definition
Act	Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010)
Code	The Bankruptcy Code
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010)
FDIC	Federal Deposit Insurance Corporation
Title II	Title II of the Dodd-Frank Act, creating the "Orderly Liquidation Authority"

SUMMARY OF ARGUMENT

The Dodd-Frank Act eliminated a substantive statutory right that the Bankruptcy Code long had bestowed upon the States and other bondholders: the right not to suffer discrimination versus similarly situated creditors. 11 U.S.C. §§ 726(b), 1123(a)(4). That right is valuable to the States and other investors not just in bankruptcy proceedings but also here-and-now: a bond *with* the Code's anti-discrimination protection offers more value to the States and other investors than does the same bond *minus* that anti-discrimination protection—and not just in future bankruptcy proceedings, but *today*. *See* States Br. 4-5, 21-27.

The enactment of Dodd-Frank's Title II stripped away that protection, by superseding it with a broad new grant of power to federal regulators to discriminate among similarly situated creditors. So as the States' statutory creditor rights had value now, Dodd-Frank's elimination of those rights injures the States now. States Br. 21-27.

The Government does not attempt to rebut the basic point, rooted in precedent and scholarship, that the Bankruptcy Code's statutory rights were of pre-bankruptcy value to creditors. Instead, the Government attempts to re-characterize the States' theory of standing as centering on "potential injury" (Gov't Br. 54), on "future injury" (*id.* at 57), or on how "investors might react" in the event of a future liquidation (*id.* at 59). But the States' injury already occurred, when Dodd-Frank

superseded statutory rights undergirding the States' investments. Terminating those rights causes injury now, regardless of whether that injury is further compounded by future financial losses.

Finally, the Government urges the Court to delay adjudication of the States' constitutional claims until liquidation occurs—but refuses to commit to the position that courts would have jurisdiction to hear such claims at that time. Gov't Br. 63. The Government's professed uncertainty here contrasts with its position in another pending case involving an identical jurisdictional statute, which it brandishes there as a "sweeping ouster" of judicial power. *Infra* Part III.B. Because Dodd-Frank prohibits creditors from litigating the States' constitutional claims once liquidation occurs, the States must raise these purely legal claims before liquidation, or never at all.

ARGUMENT

I. The States' Statutory Right Had Immediate Value

A plaintiff's injury "may exist solely by virtue of 'statutes creating legal rights, the invasion of which creates standing.'" *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 578 (1992). The Bankruptcy Code long created such a right for creditors, by protecting them against discrimination versus similarly situated creditors during bankruptcy. 11 U.S.C. §§ 726(b), 1123(a)(4).

A. The States' opening brief plainly identifies the precise statutory right that Dodd-Frank eradicates, and it traces the right's century-deep roots in federal law. States Br. 4, 21-22. It explains at length why this particular right is valuable not just in bankruptcy proceedings but also in the present, long *before* any default. *Id.* at 22-27.

The Government does not respond to that argument—it does not even cite the statutory right the States invoke. Instead, the Government attempts to re-characterize the case as concerning "a supposed statutory right to future bankruptcy proceedings." Gov't Br. 59. But the States do not claim a right to "future proceedings." Rather, they make the common-sense claim that as creditors they are injured now by Dodd-Frank's elimination of their statutory right against discrimination—a right that is valuable not just during future bankruptcy proceedings but also long before default, when States and other investors choose which investments to make, which to maintain, which to exit, and at which prices to do so. States Br. 22-27.

B. The Government's fundamental mischaracterization of the practical value of the States' lost right is highlighted by its attempt to distinguish the line-item veto case, *Clinton v. City of New York*, 524 U.S. 417 (1998), and the contractual impairment case, *U.S. Trust Co. of New York v. New Jersey*, 431 U.S. 1 (1977). The distinctions drawn by the Government reflect a myopic and mistaken

focus on future bankruptcy proceedings as the *only* circumstances in which creditors' statutory rights are valuable.

1. The Government asserts that the States' statutory rights bear "no resemblance" to the plaintiffs' interests in *Clinton v. City of New York*. Gov't Br. 60. There, a farmers' cooperative was injured by the repeal of a tax benefit the farmers hoped to realize someday. *See* States Br. 19-20. The Government argues the States lack "concrete plans to utilize the benefits" of the Bankruptcy Code, comparing them unfavorably with *City of New York*'s farmers, who had "engaged in ongoing negotiations" to buy assets favored by the repealed statutory tax subsidy, from an owner who "had expressed an interest in structuring a tax-deferred sale when the President canceled [the statute]." Gov't Br. 60 (quoting 524 U.S. at 432).

But the States were *already benefitting* from the Bankruptcy Code's anti-discrimination protection for creditors, not merely planning to do so in the future: they capitalized on the statute by purchasing bonds (and the protection they carried) instead of common stock or another less-protected investment. *See, e.g.*, States Br. 23 (quoting Benjamin Graham & David L. Dodd, Security Analysis 149 (6th ed. 2009)). The States' rights under the Bankruptcy Code are far more concrete than were the farmers' "plans." 524 U.S. at 432.

Furthermore, when the Government quotes *City of New York*'s conclusion that the farmers faced "a sufficient likelihood of economic injury,"

Gov't Br. 60 (quoting 524 U.S. at 432), it disregards the Supreme Court's actual analysis. Repealing that tax subsidy statute "depriv[ed]" the farmers "of their statutory bargaining chip." 524 U.S. 432. And that loss, not monetary losses, placed the farmers comfortably within the Supreme Court's precedents "routinely recogniz[ing] probable economic injury resulting from governmental actions that alter competitive conditions as sufficient to satisfy the Article III 'injury-in-fact' requirement." *Id.* at 432-33 (alterations omitted). The States suffer the same type of injury: when Title II stripped creditors of that statutory nondiscrimination right, it eradicated the States' statutory "bargaining chip." *See* States Br. 21-27.

2. The Government also miscomprehends *U.S. Trust*, where the Supreme Court held that bondholders' contracts were "impaired" by New Jersey's repeal of a state statute that undergirded the bonds' revenue base. The Government asserts that the Supreme Court's holding was based on "an initial adverse effect" on the price of the bonds. Gov't Br. 61 (quoting 431 U.S. at 19). But the court's analysis did not rest on the bonds' various price fluctuations, as the court makes clear in the words preceding and following its mention of "an initial adverse effect"—which the Government omits from its quote. *See* 431 U.S. at 19 ("the bonds nevertheless retained an 'A' rating from the leading evaluating services," and "they regained a comparable price position in the market"); *see also*

id. ("The fact is that no one can be sure precisely how much financial loss the bondholders suffered.").

In fact, the Supreme Court stressed that market prices would not necessarily reflect the real impact of New Jersey's repeal: "the market may not have reacted fully, even as yet, to the covenant's repeal," and "[f]actors unrelated to repeal may have influenced price." *Id.* "In any event," the court explained, "the question of valuation need not be resolved in the instant case," because the contracts' impairment was found not in lower bond prices, but in the non-quantitative impact of New Jersey's repeal: it "totally eliminated an important security provision and thus impaired the obligation of the States' contract." *Id.*

That security provision was valuable to *U.S. Trust*'s bondholders regardless of market price fluctuations. So too was the Bankruptcy Code's creditor-nondiscrimination right, an important security provision and thus a valuable component of the States' own investments.[1]

Finally, the Government scoffs that the "States conspicuously do not allege that the market value of their assets has gone down." Gov't Br. 58-59. But this disregards *U.S. Trust*'s admonition that momentary market prices are not the

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[1] "[T]he laws which subsist at the time and place of the making" of the contract "enter into and form a part of it, as if they were expressly referred to or incorporated in its terms." *Id.* at 19 n.17.

exclusive evidence of value, 431 U.S. at 19. The States' loss of a valuable statutory right, when Dodd-Frank ended the federal statutory guarantee of creditor nondiscrimination, is a judicially remediable injury regardless of whether its effect on bond prices presently can be quantified. *Zivotofsky v. Sec'y of State*, 444 F.3d 614, 619 (D.C. Cir. 2006); *cf. Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1019 n.8 (1992) (recognizing that while land has economic value, "there are plainly a number of noneconomic interests in land whose impairment will invite exceedingly close scrutiny under the Takings Clause").

II. The Government Does Not Alleviate The States' Injury By Suggesting That It Might Use Its New Discrimination Powers "Only In Certain Limited Circumstances"

When Title II was enacted to supersede the Bankruptcy Code, the States lost the protection of their statutory right. Yet the Government argues that the States suffer no injury until the Treasury Secretary orders the "liquidation" of a company and the Federal Deposit Insurance Corporation (FDIC) forces the States to incur financial losses in that liquidation. Gov't Br. 56-58.

A. The Government's logic is again belied first and foremost by *City of New York* and *U.S. Trust*. In *City of New York*, the farmers were injured by the statute's repeal *per se*; they were not forced to wait until after purchasing tax-benefitted assets and then exhausting the Internal Revenue Service process before challenging the statute's repeal in court. 524 U.S. at 432. In *U.S. Trust*, the

bondholders' contracts were impaired by the repeal of the bond-security statute *per se*; they were not forced to further prove the bonds' "impairment" with measurable price decreases or ratings downgrades, let alone to sell the bonds at a loss in order to ripen their constitutional challenges. 431 U.S. at 19.

The Government argues that *Zivotofsky* recognizes noneconomic injuries only when caused by administrative action, rather than by legislative repeal. Gov't Br. 59-60. But *Zivotofsky* did not suggest that such a loss of statutory rights creates standing *only* when an administrative agency takes away the rights—indeed, it had no occasion to suggest that. In *Zivotofsky*, Congress had not repealed the right, so only the agency's refusal to enforce the statute could injure the plaintiff. 444 F.3d at 619.[2]

Congress and agencies are each capable of stripping statutory rights—Congress by repeal, agencies by regulatory action or inaction. The Government offers no explanation why the latter injures but not the former.

B. The Government argues the States are not yet injured because the FDIC ultimately might treat them no worse than they would have been treated

[2] Furthermore, creditors' statutory rights differ substantively from *Zivotofsky*'s passport-designation right: creditors' rights are designed to affect investors long before bankruptcy occurs and government acts. States Br. 21-27.

under the previous bankruptcy regime. Gov't Br. 57. It suggests that the FDIC might discriminate "only in certain limited circumstances." *Id.* at 56.

But suggestions of administrative self-restraint are no substitute for well-established statutory rights,[3] especially when the statutes were enacted precisely to assure creditors of their rights long before bankruptcy occurs. States Br. 21-27. Creditors can hope the FDIC will not discriminate against them, but hope alone is a far cry from the enforceable legal rights they had until Dodd-Frank superseded the Bankruptcy Code.

C. The Government further belittles the Bankruptcy Code's statutory antidiscrimination rights by stressing that those rights did not singlehandedly eliminate *all* "significant uncertainties surrounding how [bondholders] would be treated as creditors in bankruptcy." Gov't Br. 58. That is a red herring. The States nowhere suggest that creditors faced *no* uncertainty in bankruptcy under the pre-Dodd-Frank regime. But amidst the general uncertainty of investments, the Bankruptcy Code provided one anchoring point of certainty—namely, that similarly situated creditors could not suffer discrimination.[4]

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[3] *Cf. Whitman v. Am. Trucking Ass'ns*, 531 U.S. 457, 472 (2001) ("We have never suggested that an agency can cure an unlawful delegation of legislative power by adopting in its discretion a limiting construction of the statute.").

[4] The two out-of-Circuit cases cited in passing by the Government do not suggest otherwise. In *In re Bonner Mall Partnership*, the Ninth Circuit simply recognized that

(*footnote continued on next page*)

The States' injury is illustrated by the Supreme Court's "bundle of rights" metaphor. *See* States Br. 24-25. The Government effectively argues that because the State bondholders' "bundle" did not include a promise of absolute certainty in bankruptcy, they cannot complain when the Government abrogates the specific rights that actually had been in the States' bundle. Like any investor, the States would love absolute certainty, coupled with high returns on their investments. But at the very least, the States valued their original bundle of rights—the ones they obtained by buying the bonds—and are injured when Title II legislates away one or more of those rights.

Finally, the Government cites the Bankruptcy Code's Section 1129(a)(7) as an example of uncertainty facing creditors in bankruptcy proceedings, Gov't Br. 58, but that statute actually supports the States' case. Bondholders in Chapter 11 reorganizations can receive less than they would have been entitled to

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the "absolute priority rule" does not prevent stockholders from receiving stock in a newly reorganized corporation, so long as those stockholders provide "new value" in the form of new capital. 2 F.3d 899, 906-07 (9th Cir. 1993); *see also id* at 906 (stressing that this doctrine "is not actually an exception to the absolute priority rule but is rather a corollary principle, or, more simply a description of the limitations of the rule itself"). Similarly, in *In re Just For Feet, Inc.*, a district court reiterated that Section 105 of the Bankruptcy Code allows Chapter 11 debtors to pay certain "pre-petition claims when such payment is deemed necessary to the survival of the debtor." 242 B.R. 821, 824 (D. Del. 1999). The FDIC's new authority to discriminate against similarly situated creditors is significantly broader, *see* 12 U.S.C. § 5390(b)(4)—and all the more so in the absence of strong judicial oversight central to traditional court-managed bankruptcy.

in Chapter 7 liquidations, if "they *agree* to a lesser amount." *Id.* (citing 11 U.S.C. § 1129(a)(7)) (emphasis added). By placing that option in the hands of the *bondholders*, the statute gave them—not the FDIC or other regulators—the power to exercise their statutory right or to bargain it away for something of value. By contrast, Title II takes that power away from bondholders and gives it to the FDIC.

D. The States' position creates no slippery slope. The States do not claim that all bondholders "have standing to challenge *any* change in the Bankruptcy Code." Gov't Br. 60 (emphasis added). The States' injury arises not from the change of non-substantive procedures, or from *de minimis* modifications of the Code, but from a fundamental change to the Code's "*central policy*" of creditor nondiscrimination. *Begier v. IRS*, 496 U.S. 53, 58 (1990) (emphasis added).

E. Finally, the claims are ripe. They present purely legal questions not contingent upon future developments; because the States challenge Title II *per se*, future administrative action would not "bring the issues into greater focus." *See* States Br. 28. Indeed, no future agency actions could cure the statute's inherent unconstitutionality, the subject of the States' claims. *Whitman*, 531 U.S. at 472-73. And the Government identifies no hardships justifying delay. *Nat'l Ass'n of Home Bldrs. v. U.S. Army Corps of Eng'rs*, 440 F.3d 459, 465 (D.C. Cir. 2006).

III. Dodd-Frank Prohibits The States From Litigating These Claims Once A Liquidation Begins

A. Dodd-Frank bars the States from litigating their constitutional claims once an "orderly liquidation" occurs. *See* States Br. 29-30. The Government nonetheless argues that the States' constitutional claims should not be adjudicated until after a Dodd-Frank liquidation occurs.

But the Government refuses to commit to the position that creditors certainly can litigate these constitutional claims in post-liquidation judicial review. Rather, the Government offers merely that "it is *difficult to know for certain* whether the States' claims could ultimately be brought under [the provision allowing judicial review of FDIC's payment decisions], or some other." Gov't Br. 63 (emphasis added).

In fact, the law is clear: the States' constitutional claims cannot be brought under "some other provision" once liquidation occurs, because Title II expressly prohibits it. 12 U.S.C. §§ 5390(a)(9)(D) & 5390(e). Title II also prevents creditors from litigating these issues in an appeal of the Treasury Secretary's original decision to liquidate the company. *See* States Br. 29-30.

Nor could the States' constitutional claims be litigated in an appeal of the FDIC's payment decisions. Section 5390(a)(4), titled "Judicial determination of claims," provides only for review of the FDIC's decisions regarding creditors' "right to payment" from the FDIC as receiver. 12 U.S.C. § 5390(a)(4); *id.* § 5381(a)(4)

(defining "claim" as "any right to payment"). This nowhere empowers the FDIC or the reviewing court to adjudicate whether Title II's "Orderly Liquidation Authority" is constitutional in the first place—let alone to provide injunctive or declaratory relief against the liquidation, which also is expressly prohibited. *See* 12 U.S.C. § 5390(e) (prohibiting injunctive and declaratory relief).[5]

Nor does Section 5390(a)(4) allow the courts to fully compensate for the actual value of losses incurred in the liquidation (such as under the Tucker Act); instead, the statute artificially caps recovery according to a strictly hypothetical inquiry into what the claimant "would" have received if the company had been liquidated, at that moment, under Chapter 7 of the Bankruptcy Code instead.[6]

In addition to those myriad statutory barriers to post-liquidation litigation, there is a practical barrier. Because courts cannot stay a liquidation while judicial review is pending, *see* States Br. 7-8, the Government could complete the

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[5] Moreover, it would be "futile" to expect an agency to competently adjudicate its own constitutionality. *Ryan v. Bentsen*, 12 F.3d 245, 247 (D.C. Cir. 1993).

[6] In a footnote, the Government claims that Section 5390(d)(2) does not cap what bondholders can recover from the FDIC. Gov't Br. 57 n.10. In fact, Section 5390(d)(2), titled "Maximum liability," provides that the FDIC's "maximum liability" to creditors and other claimants "shall equal the amount that such claimant would have received if" the FDIC had not been appointed receiver and the debtor company "had been liquidated under chapter 7. . . ." 12 U.S.C. § 5390(d)(2). And as noted in the opening brief, scholars suggest that the amount recovered by creditors, under this hypothetical fire-sale rubric, "is likely to be close to zero." States Br. 9-10.

liquidation, and moot the constitutional challenges, long before litigation is complete. This is not idle speculation—it is the fate that befell Indiana's pension fund investments in the bonds of "Old Chrysler," a year before Dodd-Frank's enactment. *Ind. State Police Pension Trust v. Chrysler LLC*, 558 U.S. 1087 (2009); Fred N. David, *Interpreting the Supreme Court's Treatment of the Chrysler Bankruptcy and Its Impact on Future Business Reorganizations*, 27 Emory Bankr. Dev. J. 25, 39 (2010).

B. Nevertheless, the Government suggests in this case that Dodd-Frank *might* not prohibit post-liquidation litigation over Title II's constitutionality. But the Government's equivocation before this Court contrasts starkly with its position in another case pending in this district, where it argues that an identical judicial review statute completely "excludes judicial review of 'the exercise of powers or functions' given to the" challenged agency, "effect[ing] a sweeping ouster of the court's power to grant equitable remedies" against the agency. Treasury Dep't Mot. to Dismiss at 22, 23, *Perry Capital LLC v. Lew*, No. 13-1025 (D.D.C. filed Jan. 17, 2014) (Docket No. 31-1), 2014 WL 298737 (quoting cases applying identical statutory language).

In *Perry Capital LLC v. Lew*, investors allege that regulators violated statutory limits on their authority as conservators of Fannie Mae and Freddie Mac. But the Government invokes a jurisdictional provision identical to Dodd-Frank's

Section 5390(e),[7] and asserts it as a "statutory bar against injunctive or other relief restraining [the agency's] powers as conservator . . . By its terms, this provision *excludes judicial review* of the exercise of powers or functions given to the [agency] as conservator." *Id.* at 22 (quotation marks omitted, emphasis added). Far from suggesting that the statute might leave the door open to judicial review, the Government urges in *Perry* that the statutory language "does indeed effect *a sweeping ouster of the court's power* to grant equitable remedies" against the government. *Id.* at 23 (quoting *Freeman v. FDIC*, 56 F.3d 1394, 1399 (D.C. Cir. 1995) (another identical statute) (emphasis added).

The States must litigate their constitutional claims now, before a Dodd-Frank liquidation triggers another "sweeping ouster of the court's power." The States are injured. Their claims are ripe for review.

CONCLUSION

The judgment of the district court should be reversed.

[7] *Compare* 12 U.S.C. § 5390(e) ("no court may take any action to restrain or affect the exercise of powers or functions of the receiver hereunder"), *with* 12 U.S.C. § 4617(f) ("no court may take any action to restrain or affect the exercise of powers or functions of the Agency as a conservator or a receiver").

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STATEMENT PURSUANT TO D.C. CIRCUIT RULE ECF-3

Pursuant to D.C. Circuit Rule ECF-3(B), the undersigned certifies that counsel for all of the State Plaintiffs-Appellants consent to the filing of this brief.

April 28, 2014

/s/ Patrick Wyrick
Patrick Wyrick

CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B)(i), and the order of this court dated December 20, 2013 [Dkt. #1471629], because the brief contains 3,490 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

This brief complies with typeface requirements of Fed. R. App. P. 32(a)(5) and the type-style requirements of Fed. R. App. P. 32(a)(6), because it has been prepared in a proportionally spaced typeface using Microsoft Word in Baskerville 14-point font.

April 28, 2014

/s/ Patrick Wyrick
Patrick Wyrick

CERTIFICATE OF SERVICE

I hereby certify that all counsel of record who have consented to electronic service are being served today with a copy of this document via the Court's CM/ECF. All parties in this case are represented by counsel consenting to electronic service.

April 28, 2014

/s/ Patrick Wyrick
Patrick Wyrick